

Friday, July 2, 2010

Fercroft occupancy woes raise default concerns

Boston Business Journal - by [Craig M. Douglas](#)

The Fercroft Corporate Center in Middleton has historically thrown off close to \$225,000 in cash each month, but the property's owner of record, a real estate investment trust run by Dallas-based Behringer Harvard, hasn't been able to touch a dime of it in weeks.

Since April, the **Behringer Harvard Opportunity REIT I** has been operating under a cash-management arrangement with the property's special loan servicer, LNR, due to a "significant drop in occupancy" that has raised the potential for an "imminent default" and possible foreclosure, according to regulatory and financial filings.

The REIT recorded a \$4.2 million impairment charge related to the Fercroft property in the first quarter, shortly before analysts raised red flags over the \$18 million loan backing the site. The investment firm later confirmed in regulatory filings that despite Fercroft's record of relatively healthy cash flow, it was negotiating with LNR to potentially modify its loan or sell the property outright.

The clock could be close to expiring on both potential outcomes. In a May 25 note to investors, Behringer Harvard said its plan to rework the loan had been rejected. Barring a last-minute sale, the firm said it was likely to hand over the keys by the end of this week.

Behringer Harvard declined to comment, but did confirm that it still owned Fercroft as of late June. The firm's recent problems came to light earlier this year when its two largest tenants renewed leases at lower rents and for 60,000 square feet less space.

"The Fercroft loan is non-recourse to us," Behringer Harvard wrote in a recent filing with the **Securities and Exchange Commission**, adding "... there is no certainty to which outcome from the negotiations will prevail."

The firm also warned that its so-called lockbox provision is only adding to its problems, as access to cash is needed to stay compliant with its loan arrangement.

Legal and real estate experts say such lockbox accounts have become increasingly common — albeit controversial — among lenders fearful over distressed properties. Lockbox provisions are generally triggered by an event specified in the original loan agreement and are seen as a layer of insurance for lenders concerned over the upkeep of their secured properties. It's also a way to prevent underwater borrowers from siphoning off cash for other unrelated needs.

"Usually a lockbox is only put in place when a default has occurred," said Zev Gewurz, the director of **Goulston & Storrs'** real estate group. He said lockbox provisions can "reverse out" if a borrower's financial footing stabilizes, and property owners have a right to claim any excess cash-flow above a property's debt service and operating expenses.

Beyond that, borrowers are generally at the mercy of whomever controls the lockbox funds. Sometimes it is the special servicer assigned to the loan; most often it's the lender. Gewurz said the situation can often lack a sense of urgency, once a property's cash-flow has been redirected in favor of a lender. Frustrated property owners are usually left to stew.

"They're stuck in this situation where they're not getting any cash but they still have the burden of managing the property," he said. "They're carrying this liability and all they want is to give back the keys."

Investors in Behringer Harvard's Opportunity REIT I would likely welcome some clarity on the Fercroft matter. The property's first quarter writeoff accounted for around a third of the fund's \$13.2 million net loss for the period.

Meanwhile, the REIT has around \$200 million in debt scheduled to mature before Dec. 31.

As of March 31, Opportunity REIT I had \$748.9 million in assets, an 11 percent drop from the \$843.9 million on its books at the end of 2009. Most of that change was attributable to a decrease in its real estate holdings, according to the firm's financial filings.

Built in 1990, the Fercroft Corporate Center's largest tenants include **Verizon Inc.** spinout **SuperMedia Inc.**, which produces online and printed phone directories, and the **SAS Institute Inc.**, a developer of business software. Behringer Harvard acquired the 226,338-square-foot office site for \$27 million in mid 2006.

An SAS Institute spokeswoman confirmed this week that the North Carolina company extended its Fercroft lease, originally set to expire Aug. 31. She declined to say whether the agreement was for the same 55,800-square-foot space.

"SAS has a significant investment in Middleton, with more than 100 employees and a data center. We are committed to maintaining our presence there, as evidenced by the extension of our lease," said Beverly Brown, the spokeswoman.



[View Larger](#)